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No. 797

In the Supreme Court of the United States

OCTOBER TERM, 1959

WOOD-MOSAIC COMPANY, ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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OPINIONS BELOW

The opinion of the District Court for the Western District of Kentucky (Pet. 17–25) is reported at 160 F. Supp. 631. The *per curiam* opinion of the court of appeals (Pet. 17) is reported at 272 F. 2d 944.

JURISDICTION

The judgment of the court of appeals was entered on December 22, 1959 (Pet. 17). The petition for certiorari was filed on March 17, 1960. The jurisdiction of this Court is invoked under 28 U.S.C. 1254.

QUESTION PRESENTED

Whether a corporation, which acquired substantially all of the operating assets of another corporation in

exchange for all of its stock, is a new corporation, within the meaning of the excess profits tax statute.

STATUTES INVOLVED

The relevant provisions of the Internal Revenue Code of 1939, Sections 435(b), 445 (a) and (g), 461 (a), (b) and (d), and 462(g), are printed in the Appendix, *infra*, pp. 8–11.

STATEMENT

This case, arising out of suits for refund of excess profits taxes for the years 1951, 1952, and 1953, involves two corporate taxpayers—Wood-Mosaic Corporation, hereafter referred to as the "Corporation," and Wood-Mosaic Company, hereafter referred to as the "Company." The Corporation has been engaged in substantially the same business continuously since 1907. The Company was incorporated on November 28, 1947. On December 1, 1947, the Corporation transferred its operating assets and manufacturing facilities located in the United States to the Company and, in consideration of the transfer, received all of the outstanding and issued capital stock of the Company (Pet. 17–18).

The Commissioner determined that the Company was not a new corporation within the meaning of the excess profits tax provisions of the Internal Revenue Code of 1939, but instead was an acquiring corporation with the base period of its predecessor, and assessed taxes accordingly. The Commissioner also determined that, within the meaning of the Code, the Corporation was a "component" corporation which

had surrendered its base period with respect to the assets transferred to the Company. The taxpayers paid the taxes as assessed by the Commissioner and sued for refunds on the theory that the Company was a "new corporation" within the meaning of Section 445 of the Internal Revenue Code of 1939, Appendix, *infra*, p. 8. The taxpayers also contended that the Corporation was entitled to use the base period earning experience of the assets transferred to the Company, which would result in no excess profits tax to it (Pet. 18, 22–23).

The two refund suits were tried jointly (Pet. 17). The district court upheld the Government on both issues (Pet. 21–25), and the court of appeals affirmed upon the findings of fact and conclusions of law of the district court (Pet. 17).

ARGUMENT

The question presented involves the interpretation of certain provisions of the Excess Profits Tax Act of 1950, c. 1199, 64 Stat. 1137, which became effective on January 3, 1951, as a part of the Internal Revenue Code of 1939 (Subchapter D of Chapter I, Sections 430–472). The decision below correctly construes the statute in accordance with its express terms, no conflict exists, and there is no other reason for further review. The question does not have any future public importance, since by its terms the excess profits tax is not imposed for taxable years beginning on or after January 1, 1954 (Section 430(a)).

Section 445 provides a preferential excess profits credit for a new corporation. The preferential credit

is computed by using a prescribed average rate of return on invested capital for classified industries, upon the assumption that a new corporation has no prior business experience or base period on which actual average earnings can be computed. Section 445(a), Appendix, *infra*, p. 8, defines a new corporation as a corporate taxpayer "which commenced business after the first day of its base period", which is fixed for the facts of this case by Section 435 (b), Appendix, *infra*, p. 8, as January 1, 1946. While the critical phrase "commenced business' is not defined in Section 445 itself, it is defined by Section 461 in Part II of the excess profits tax provisions. Section 461(a), Appendix, *infra*, p. 10, defines an acquiring corporation as one which, in exchange for all of its stock, has acquired all of the properties of another or a "component corporation." See Section 461(b), Appendix, *infra*, p. 10. Section 461(d), Appendix, *infra*, pp. 10–11, provides that for the purposes of Section 445 (and other prior sections) any taxpayer which is an acquiring corporation "shall be considered to have commenced business on the earliest date on which it or any of its component corporations commenced business." Section 461(d) goes on to provide that the component corporation shall not be deemed, for the purposes of Section 445, to have commenced business prior to the acquistion. Moreover, Section 462(g), Appendix, *infra*, p. 11, which deals with the application of the preferential credit for new corporations provided in Section 445 to Part II transactions, provides that an acquiring corporation, which by virtue of Section 461(d) commenced business before

January 1, 1946, "shall not be entitled to compute its average base period net income under section 445 * * *."[1]

The Company in this case is clearly an acquiring corporation and the Corporation is a component corporation. Therefore, by virtue of the express provisions of the statute, the Company is not a new corporation, but is required to use the experience of its predecessor in computing its excess profits credit. Moreover, under Section 461(d) the Corporation has surrendered the earnings experience of the transferred assets to the Company.

The taxpayers' contention (Pet. 13)—that they can elect whether to proceed under Section 445 or Section 461 since the latter section is not mandatory—is contrary to the express terms of Section 461. The statute adopts the not unusual procedure of defining in one section the terms used in another, and describing the scope of the definition in the defining, rather than in the defined, section. Therefore, the taxpayers are mistaken in claiming that Section 445 can be read without reference to Section 461 so that any corporation which was organized after January 1, 1946, but which acquires a prior business, is a new corporation for the purposes of Section 445, unless it is excepted by Section 445(g).

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[1] The House and Senate Committee Reports simply restate the express language of the statutory provisions. H. Rep. No. 3142, 81st Cong., 2d Sess., pp. 63–64 (1951–1 Cum. Bull. 187, 231–232); S. Rep. No. 2679, 81st Cong., 2d Sess., p. 38 (1951–1 Cum. Bull. 240, 266). The Treasury Regulations 130, Sections 40.461–1 and 40.461–4, added by T. D. 5865, 1951–2 Cum. Bull. 97, are consistent with the express statutory language described above.

Section 445(g), Appendix, *infra*, p. 9, on its face applies only to transactions taking place after December 1, 1950, covers transactions other than acquisitions defined in Section 461, and in no way qualifies the application of the Section 461 definition of "commenced business" to Section 445(a). Thus, far from rendering various portions of the statute inconsistent with each other as the taxpayers claim (Pet. 13), the analysis of the statute which we have made above is the only one in accord with its express terms.

Phinney v. *Tuboscope Co.*, 268 F. 2d 233 (C.A. 5), upon which the taxpayers rely to show a conflict (Pet. 13), is actually in accord with the decision below, since it holds (1) that the definitions in one section of the excess profits tax provisions of the 1939 Code apply to another by "the shorthand method of incorporation by reference" (*id.* at 236); (2) that Section 445(g) covers transactions that "would not meet the definition of an acquiring corporation under Section 461" (*id.* at 237); and (3) that, as a matter of principle, the benefit of the favorable excess profits credit for new corporations is not conferred upon the "continuation of a long existing organization and business" under a new corporation shell (*id.* at 239). See also *General Retail Corp.* v. *Commissioner*, 262 F. 2d 591 (C.A. 6), affirming 29 T.C. 632, certiorari denied, 360 U.S. 918.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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MAY 1960.

APPENDIX

Internal Revenue Code of 1939:

SEC. 435 [as added by Sec. 101, Excess Profits Tax Act of 1950, c. 1199, 64 Stat. 1137]. EXCESS PROFITS CREDIT—BASED ON INCOME.

* * * * *

(b) *Base Period.*—As used in this subchapter the term "base period" means the period beginning January 1, 1946, and ending December 31, 1949, except that in the case of a taxpayer whose first taxable year under this subchapter was preceded by a taxable year which ended after December 31, 1949, and before April 1, 1950, and which began before January 1, 1950, the term "base period" means the period of 48 consecutive months ending with the close of such preceding taxable year.

* * * * *

(26 U.S.C. (1952 ed.) 435)

SEC. 445 [as added by Sec. 101, Excess Profits Tax Act of 1950, *supra*]. AVERAGE BASE PERIOD NET INCOME—NEW CORPORATION.

(a) *New Corporation.*—A taxpayer which commenced business after the first day of its base period shall, except as provided in subsection (g), be considered a new corporation for the purposes of this section, and its average base period net income determined under this section shall be the amount computed under subsection (b).

* * * * *

(g) *Ineligible Corporations.*—

(1) If a taxpayer, on or after December 1, 1950, and prior to the end of its third taxable year, acquires any properties in any of the transactions described in paragraph (2), it shall not, for the taxable year in which such acquisition occurs or for succeeding taxable years, be entitled to the benefits of this section except under the circumstances and subject to the limitations provided in section 462(g).

(2) The transactions to which paragraph (1) applies are as follows:

(A) The acquisition by the taxpayer from another corporation of properties the basis of which in its hands is determined by reference to the basis of such properties to the transferor;

(B) The acquisition by the taxpayer of a substantial part of its assets from another corporation, or of a substantial part of the properties of another corporation, if 50 per centum or more in value of the outstanding stock or outstanding voting stock of the taxpayer is directly or indirectly owned, at the time of such acquisition, by individuals owning directly or indirectly 50 per centum or more in value of the outstanding stock, or outstanding voting stock of the transferor;

(C) The acquisition by the taxpayer of a substantial part of the properties distributed on or after December 1, 1950, by another corporation, if such properties constituted a substantial part of the business assets of such other corporation, and if 50 per centum or more in value of the outstanding stock or outstanding voting stock of the taxpayer is owned directly or indirectly by individuals who at the time of such distribution owned directly or indirectly 50 per centum or more in value of the outstanding stock or outstanding voting stock of such other corporation;

(3) For the purposes of this subsection, the provisions of section 503 shall be applicable in the determination of ownership of stock.

* * * * *

(26 U.S.C. (1952 ed.) 445)

PART II [as added by Sec. 101, Excess Profits Tax Act of 1950, *supra*]—EXCESS PROFITS CREDIT BASED ON INCOME IN CONNECTION WITH CERTAIN EXCHANGES

SEC. 461. DEFINITIONS.

For the purposes of this Part—

(a) *Acquiring Corporation.*—The term "acquiring corporation" means—

(1) A corporation which has acquired—

(A) substantially all the properties of another corporation and the whole or a part of the consideration for the transfer of such properties is the transfer to such other corporation of all the stock of all classes (except qualifying shares) of the corporation which has acquired such properties, or

* * * * *

(b) *Component Corporation.*—The term "component corporation" means—

(1) In the case of a transaction described in subsection (a)(1), the corporation which transferred the assets;

* * * * *

(d) For purposes of sections 435(e), 442, 443, 444, 445, and 446, any taxpayer which is an acquiring corporation shall be considered to have been in existence and to have had taxable years for any period during which it or any of its component corporations was in existence, and such corporation shall be considered to have commenced business on the earliest date on which it or any of its component corporations commenced business. Except for purposes of the previous sentence, a component corporation

in a transaction described in subsection (a), other than one described in subsection (a)(1)(E), shall be deemed not to have been in existence or to have commenced business prior to the day after such transaction for purposes of determining the applicability of sections 435(e), 442, 443, 444, 445, and 446, to such corporation after such transaction. * * *

* * * * *

(26 U.S.C. (1952 ed.) 461)

SEC. 462. AVERAGE BASE PERIOD NET INCOME—DETERMINATION.

* * * * *

(g) *Use by Acquiring Corporation of Alternative Average Base Period Net Income Provided for New Corporations in Section 445.*—

* * * * *

(3) In the case of a transaction described in section 461(a) where the acquiring corporation had commenced business, within the meaning of section 461(d), prior to the beginning of its base period, the acquiring corporation shall not be entitled to compute its average base period net income under section 445 in the manner provided therein or as provided in this section. * * *

* * * * *

(26 U.S.C. (1952 ed.) 462)

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